

MEMORANDUM

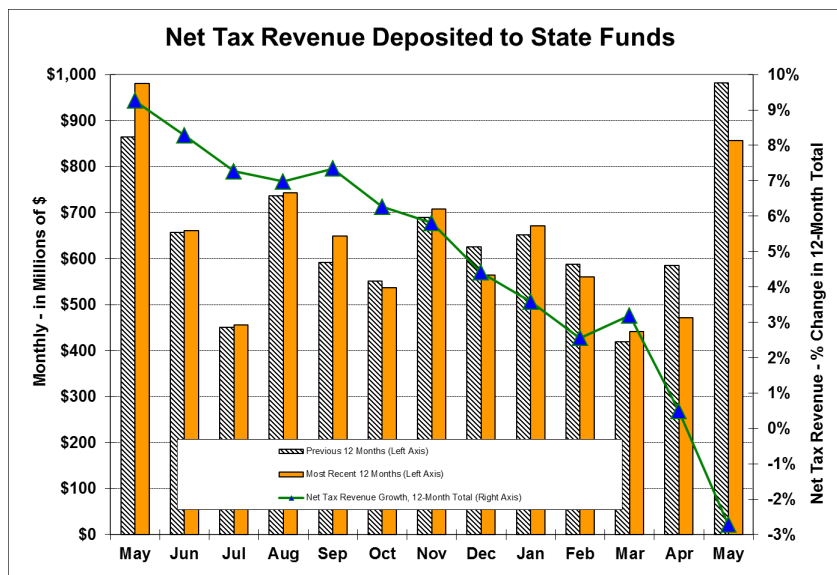
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: June 30, 2014

Twelve-month Total Net Tax Receipts Through May 31, 2014

The attached spreadsheet presents net tax revenue deposited to State funds for the 12-month period ending May 2014 with comparisons to the previous 12 months. May 2013 to May 2014 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



Overview of Current Situation

The 12-month period ending May 2013 produced net State tax revenue growth of positive 9.3%. Over the 12 succeeding months, annual revenue growth turned to a decline of 2.7%. Although much of the reversal can be traced to individual income tax changes at the State and federal level, taxes paid by banks, corporations, and casinos have also contributed to the downturn. With the processing of tax year 2013 individual returns nearly complete, the growth drag from that source should now be over.

Month of May Comparison

May net tax receipts totaled \$856.8 million, a decrease of \$124.4 million (- 12.7%) compared to May 2013. Major taxes and their contribution to the month's change include:

- Individual Income Tax (negative \$130.1 million, - 25.6%) – Individual income tax deposits, net of tax refunds issued during the month, declined significantly when compared to May 2013. Last year's State income tax returns showed significant growth, with much of that growth attributed to federal tax legislation enacted January 1, 2013. This year, individual income taxes returned to a more normal level, and a May 2014 decline is part of the result.
- Sales/Use Tax (positive \$1.0 million, 0.3%)
 - Road Use Tax Fund use tax (fee for new vehicle registration) increased \$2.7 million.
 - General Fund sales/use tax receipts decreased \$1.7 million. Gross sales/use tax receipts increased \$4.2 million while regular tax refunds increased \$0.3 million and school infrastructure transfers out increased \$5.6 million.
- Corporate Income Tax (negative \$2.6 million, - 7.5%) – Deposits for the month were down \$17.2 million while corporate tax refunds decreased \$14.6 million.
- Fuel Tax (positive \$7.9 million, 23.4%) – For the month of May, gross deposits increased \$5.0 million while fuel tax refunds decreased \$2.9 million.
- Cigarette and Tobacco Taxes (positive \$0.8 million, 3.9%)
- Gambling Tax (negative \$0.4 million, - 1.3%)

Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending May 2014, net revenue from all taxes deposited to State funds totaled \$7.316 billion, a decrease of \$205.2 million (- 2.7%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$236.4 million, - 6.9%) – Annual individual income tax growth peaked at \$451.4 million for the 12 months ending June 2013. Growth has declined steadily since that time. Due to an increase in the Iowa Earned Income Tax Credit, the new Taxpayer Trust Fund Tax Credit, and to the FY 2013 one-time boost to revenue that was the result of federal tax changes enacted January 1, 2013, the annual rate of income tax revenue growth declined significantly over the past several months.
- Sales/Use Tax (positive \$81.9 million, 3.4%).
- Corporate Income Tax (negative \$26.7 million, - 6.1%) – Corporate income tax has been volatile in recent months and trending lower, but annual income remains modestly below its all-time high.
- Bank Tax (negative \$8.2 million, - 21.3%) – The State tax paid by banks and credit unions peaked at \$42.2 million for the 12 months ending September 2013. The revenue source has declined 28.1% since that time to \$30.3 million for the 12 months ending May 2014.
- Fuel Tax (positive \$7.9 million, 1.8%) – According to Department of Revenue monthly fuel sales reports, over the most recent 12-month period, Iowa taxable gasoline/ethanol gallons sold increased 1.7%. Taxable diesel sales increased 5.1%. The annual total for all taxable fuel gallons sold in Iowa is currently 1.7% below the last peak (12 months ending July 2011).
- Gambling Tax (negative \$6.9 million, - 2.3%) – According to Racing and Gaming Commission statistics, 16 of Iowa's 18 casino/track locations recorded negative annual adjusted gross revenue (AGR) growth for the 12 months ending May 2014. The combined AGR change for the 18 facilities was negative 3.6% over the previous 12 months. Across all facilities, the AGR for the most recent 12 months totaled \$1.395 billion. The annual AGR total has been declining and is 5.1% below the November 2012 peak.

- Real Estate Transfer Tax (negative \$0.1 million, - 0.5%)
- Cigarette and Tobacco Tax (negative \$5.0 million, - 2.2%)

Tax Spotlight – Franchise (Bank) Tax and Credit Union Tax

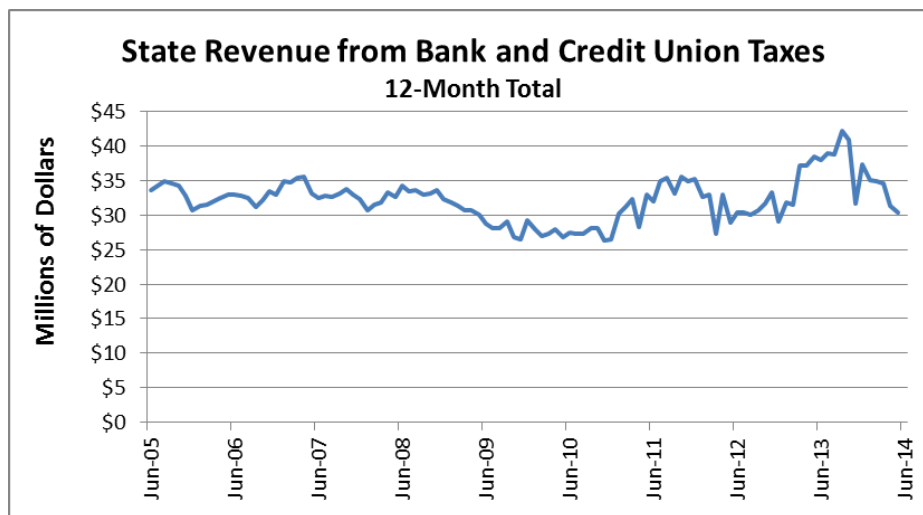
The taxation of banks and financial institutions in Iowa dates back to at least 1851. Prior to HF 1294 (Taxation of Financial Institutions Act of 1970), the bank tax was essentially a property tax, collected and retained at the local level.

The current franchise tax ([Iowa Code Chapter 422, Division V](#)) is imposed on the net income of state banks, national banking associations, trust companies, federal, and state-chartered savings and loan associations, financial institutions chartered by the Federal Home Loan Bank Board and production credit associations at a rate of 5.0%. An alternative minimum tax may be applicable to financial institutions at an effective rate of 3.0%. Credit unions are subject to a different tax discussed below.

The Iowa franchise tax enacted in 1970 provided for rates ranging from 5.0% to 8.0% of net income. The franchise tax rate was reduced to a flat 5.0% in 1980. Prior to 1995, financial institutions could transfer income-producing assets to nonbank subsidiaries reducing the franchise tax owed. Legislation was enacted beginning with tax year 1995 that prohibits the deduction of those types of transfers.

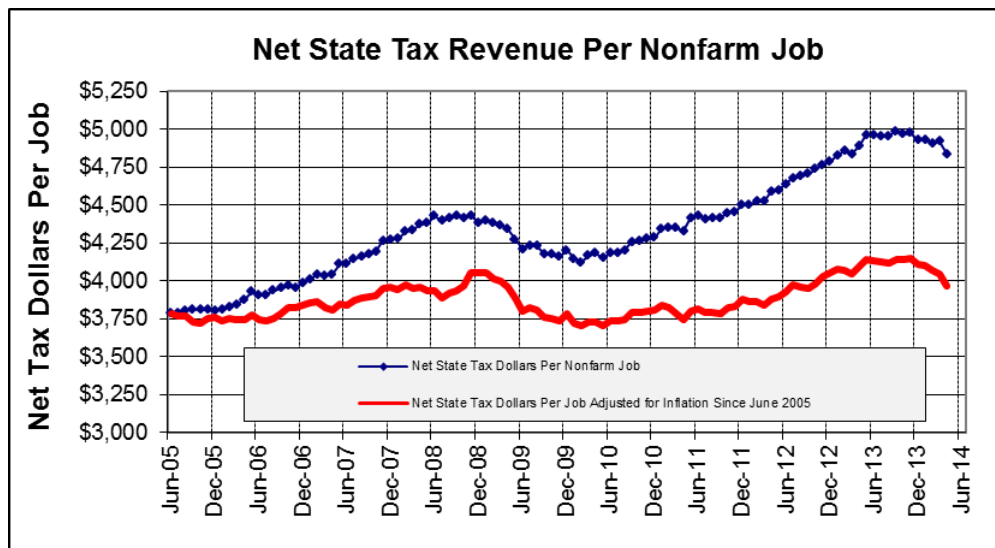
Tax returns for franchise tax are required to be filed by the last day of the fourth month after the end of the tax year. Estimate payments from most financial institutions are due on a quarterly basis. Revenue received from the franchise tax is deposited in the State General Fund.

Credit unions are taxed at a rate of five mills (0.5%) of “legal and special reserves” (see [Iowa Code Section 533.329](#)). The tax is imposed by the County Board of Supervisors and the revenue from the tax is divided between the county, city, and State, with the State share equal to 50.0% of revenue collected. The State revenue is deposited to the General Fund.

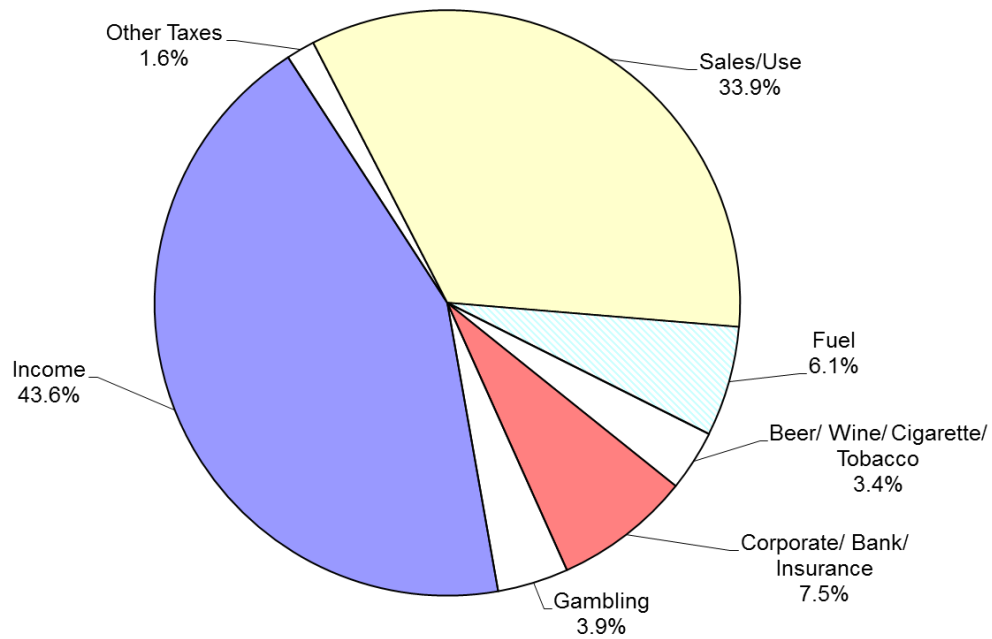


Tax Revenue and Employment

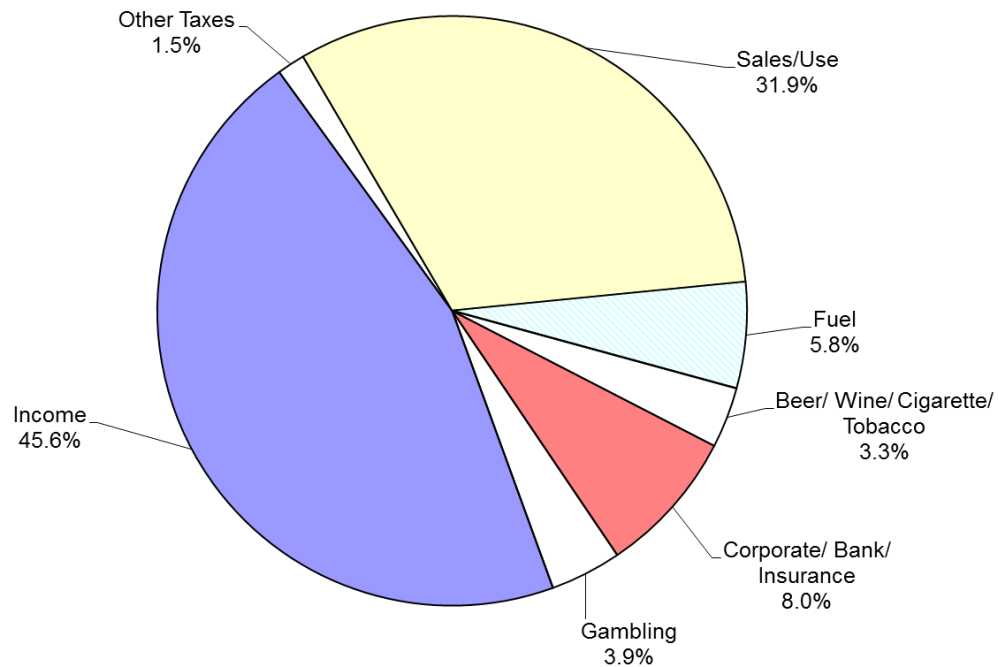
The average reading for Iowa nonfarm employment over the 12 months ending April 2014 is 1,537,700 and net State tax receipts over the same 12 months totaled \$7.440 billion, or \$4,838 per nonfarm job. This is \$1,053 higher than the per-job average for the 12 months ending June 2005. The blue line on the following chart depicts the annual tax revenue collected by the State per job, calculated monthly. The red line subtracts the impact of inflation since June 2005 from the blue line. The red line indicates that inflation adjusted tax revenue per job has increased \$184 since June 2005 and the remainder of the \$1,053 increase (\$869) represents the impact of inflation.



Net State Tax Revenue - Twelve Months Ending May 2014
Net Revenue = \$7.316 Billion
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending May 2013
Net Revenue = \$7.521 Billion
Percentages may not add to 100% due to rounding



Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of May 2013	Month of May 2014	May \$ Change	May % Change
Banking	\$ 38.5	\$ 30.3	\$ - 8.2	-21.3%	\$ 4.3	\$ 3.3	\$ - 1.0	-23.3%
Beer & Wine	22.0	22.0	0.0	0.0%	1.8	1.9	0.1	5.6%
Cigarette & Tobacco	228.6	223.6	- 5.0	-2.2%	20.5	21.3	0.8	3.9%
Corporate Income	441.3	414.6	- 26.7	-6.1%	34.7	32.1	- 2.6	-7.5%
Fuel	437.0	444.9	7.9	1.8%	33.7	41.6	7.9	23.4%
Gambling	293.8	286.9	- 6.9	-2.3%	29.8	29.4	- 0.4	-1.3%
Individual Income	3,427.7	3,191.3	- 236.4	-6.9%	508.9	378.8	- 130.1	-25.6%
Inheritance	86.3	84.6	- 1.7	-2.0%	7.4	4.0	- 3.4	-45.9%
Insurance	119.0	107.0	- 12.0	-10.1%	26.3	28.2	1.9	7.2%
Other Taxes	10.3	12.3	2.0	19.4%	0.0	- 0.1	- 0.1	-
Real Estate Transfer	18.9	18.8	- 0.1	-0.5%	1.4	2.9	1.5	107.1%
Sales/Use	2,397.4	2,479.3	81.9	3.4%	312.4	313.4	1.0	0.3%
Total Net Taxes	\$ 7,520.8	\$ 7,315.6	\$ - 205.2	-2.7%	\$ 981.2	\$ 856.8	\$ - 124.4	-12.7%
Gross Tax & Refunds								
Gross Tax	\$ 8,801.7	\$ 8,776.6	\$ - 25.1	-0.3%	\$ 1,093.8	\$ 956.3	\$ - 137.5	-12.6%
Tax Refunds	\$ - 1,280.9	\$ - 1,460.8	\$ - 179.9	14.0%	\$ - 112.7	\$ - 99.5	\$ 13.2	-11.7%
Net Tax Receipts by Fund								
State General Fund (GF)	\$ 6,381.5	\$ 6,020.2	\$ - 361.3	-5.7%	\$ 886.6	\$ 730.5	\$ - 156.1	-17.6%
Road Use Tax Fund	\$ 757.7	\$ 783.3	\$ 25.6	3.4%	\$ 64.1	\$ 74.7	\$ 10.6	16.5%
Non-GF Gambling	\$ 251.1	\$ 285.2	\$ 34.1	13.6%	\$ 29.5	\$ 29.3	\$ - 0.2	-0.7%
Other State Funds	\$ 130.6	\$ 227.1	\$ 96.5	73.9%	\$ 1.0	\$ 22.3	\$ 21.3	2130.0%
Local Option Taxes *	\$ 872.3	\$ 906.4	\$ 34.1	3.9%	\$ 79.4	\$ 106.6	\$ 27.2	34.3%

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

A percentage change displayed as "--" represents instances where the base year net revenue amount was zero or negative so no meaningful percentage change can be calculated.

Tax Categories Used in Table

Franchise (Bank) Tax: The franchise tax paid by banks is deposited in the State General Fund. Credit unions are taxed under a different system than banks, but the credit union tax is included in this line also. Of the total deposited, the bank tax provides approximately 98.0% of the revenue and the credit union tax 2.0%.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited in the State General Fund, the Liquor Control Fund, and a small amount is deposited in an Iowa Economic Development Authority fund for wine promotion.

Cigarette & Tobacco Tax: Prior to July 1, 2011, all cigarette and tobacco products tax revenue was deposited to the State General Fund. Beginning FY 2012, the first \$106.0 million of revenue from cigarette and tobacco taxes is deposited to the Health Care Trust Fund and the remainder is deposited to the State General Fund. Beginning FY 2014, all cigarette and tobacco tax revenue is deposited to the Health Care Trust Fund.

Corporate Income Tax: All corporate income tax is deposited in the State General Fund.

Motor Vehicle Fuel Tax: All motor vehicle fuel tax is deposited in one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: Gambling tax is deposited in several State funds. For FY 2013, \$40.0 million was deposited to the General Fund and the remainder to other State funds. Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, the County Endowment Fund, the Vision Iowa Fund, the Revenue Bond Debt and Subsidy Holdback Funds, the Technology Reinvestment Fund, and the Iowa Skilled Worker and Job Creation Fund.

Individual Income Tax: Most individual income tax revenue is deposited in the State General Fund. A total of \$4.0 million per year is deposited in the Workforce Development Fund. An annual \$2.6 million diversion to the Child Daycare Fund ended in FY 2009. In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited in a State fund. That revenue is not included here.

Inheritance Tax: All inheritance tax is deposited in the State General Fund.

Insurance Premium Tax: All insurance premium tax is deposited in the State General Fund.

Other Taxes: Other taxes include brucellosis eradication property tax (deposited in a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

Real Estate Transfer Tax: Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The distribution of State portion of real estate transfer tax revenue is currently changing each fiscal year, with the State General Fund portion reduced to 65.0% by FY 2015. The portion not deposited to the State General Fund is deposited to the Housing Trust Fund and the Shelter Assistance Fund.

Sales/Use Tax: General sales/use tax is deposited in the State General Fund, while most vehicle use tax is deposited in the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax is referred to as a fee in the Iowa Code. To allow continuity of data, the revenue from the fee is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted from State revenue as part of the net sales/use tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Beginning FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

Report Database: The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.